



# Economic Indicators

Prepared by the Department of Finance • June 2004

*The purpose of this report is to keep policy makers apprised of changes in the national and local economies that the Montgomery County Department of Finance believes may impact current and/or future revenues and expenditures.*



*This report is also available through the Internet  
on the Montgomery County Web Page:  
<http://www.montgomerycountymd.gov>*

*For questions regarding this report, please contact:*

*David Platt  
Chief Economist  
Montgomery County Department of Finance  
255 Rockville Pike, Suite L-15  
Rockville, Maryland 20850*

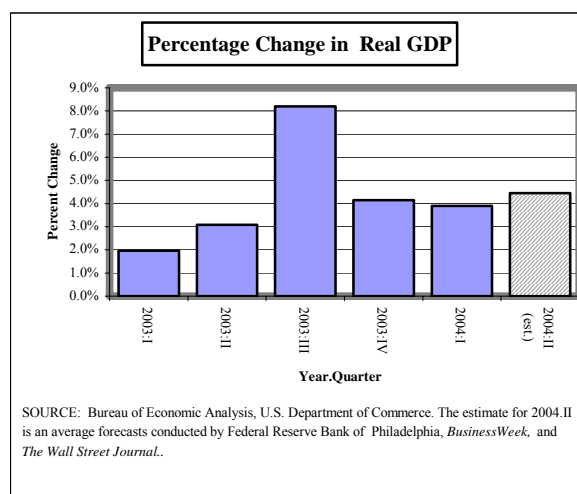
*Phone: (240) 777-8866  
Fax: (240) 777-8954  
Email: [David.Platt@montgomerycountymd.gov](mailto:David.Platt@montgomerycountymd.gov)*

## ECONOMIC OVERVIEW

According to the latest economic data, the U.S. economy continued to expand during the first quarter of 2004 albeit at a slightly lower rate compared to the second half of 2003. Based on revised data from the Bureau of Economic Analysis, U.S. Department of Commerce, real gross domestic product (GDP) grew 3.9 percent during the first quarter compared to 8.2 percent during the third quarter and 4.1 percent during the fourth quarter of 2003. Since October of last year, the economy appears to have attained a sustainable growth pattern of four percent.

Recent forecasts by the Federal Reserve Bank of Philadelphia, *Business Week*, and *The Wall Street Journal*, suggest that the economy grew 4.5 percent during the second quarter. Economic indicators for the second quarter compared to the first quarter support such forecasts. Industrial production was up 5.5 percent and the economy added 781,000 new payroll jobs. Consumer confidence, as measured by the Conference Board, was up 4.8 percent over the previous quarter. Sales of existing single-family homes increased 8.0 percent to 6.7 million units and sales of new single-family homes increased 6.6 percent to approximately 1.3 million units. According to the Mortgage Bankers Association, housing starts for single-family homes were up 3.6 percent during the second quarter. Data for retail sales and inflation provided mixed results. Retail sales up 1.4 percent but lower than the 2.3 percent growth during the first quarter. The Consumer Price Index less food and energy, or the “core” inflation, increased 2.3 percent (at an annual rate) compared to the 2.9 percent rate for the first quarter. However, two other measures of inflation less the volatile food and energy sectors, the personal consumption expenditure (PCE)

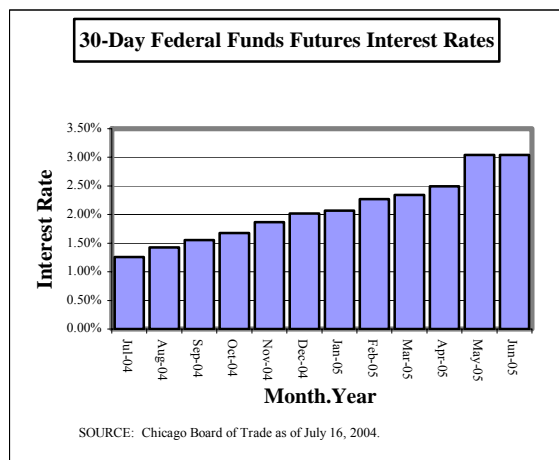
index (↑ 2.7%) and producer price index (↑ 2.9%), were higher during the second quarter compared to the first quarter (↑ 2.1% and ↑ 2.1%, respectively). With industrial production up, payroll employment increasing, a slight pick up in inflation as measured by the PCE and producer price indices, and the housing industry exhibiting strength remaining strong, the economy is expected to have outperformed the first quarter yet maintaining a sustainable pattern with a modest increase in inflation.



With the growth in payroll employment and a modest spurt in inflation during the second quarter, the focus of economic analysts is on the future actions of the Federal Open Market Committee (FOMC) of the Federal Reserve. While inflation picked up during the second quarter, the fear that inflation may accelerate was of concern to many analysts and members of the FOMC. Such concerns about inflation and the growth in employment led the FOMC to raise the target rate on federal funds from 1.00 percent to 1.25 percent in June, which was the first increase in four years. Analysts further predict that the FOMC will gradually raise the target rate on the federal funds by 225 basis points over the next twelve to eighteen months. Such increases would bring the federal funds rate to its

normal or neutral level of two percentage points above the rate of inflation. Given that the FOMC monitors the price index for personal consumption expenditures excluding food and energy as the measure of inflation and its relationship to the real interest rate of 2 percent, analysts predict that the target rate could increase from its current rate of 1.25 percent to approximately 3.50 percent by December 2005.

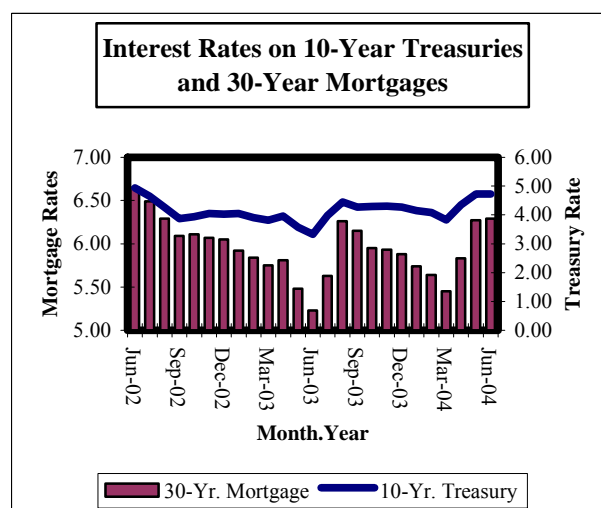
Based on data from the Chicago Board of Trade (as of July 16, 2004), the futures market for 30-day federal funds expects the FOMC to gradually raise the target rate to 3 percent by May of next year. The futures market also anticipates on average a 25 basis point increase in the target rate following each scheduled meeting of the FOMC between August and May 2005.



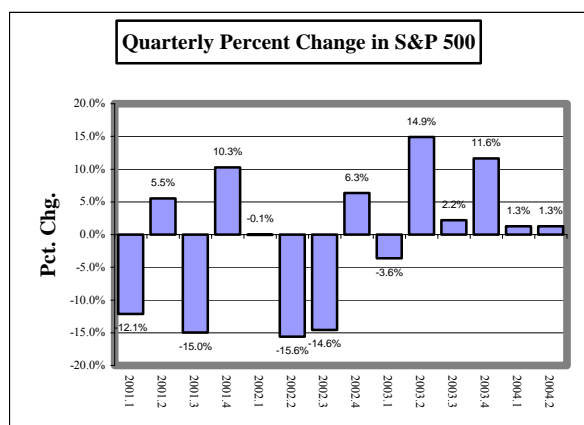
While the employment and consumer price reports released by the Bureau Labor Statistics, U.S. Department of Labor, in July showed a moderation in jobs growth and inflation, recent fears by analysts of a rapid increase in the target rates by the FOMC, both in the size of the increases and in their frequency, has subsided in recent weeks. If increases in employment and consumer prices in July and August do not exceed the

increases experienced in June, the probability that the FOMC will raise the federal funds rate in August is lessened.

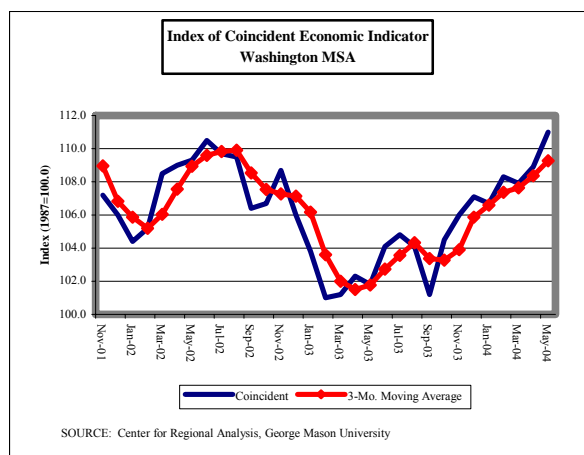
Concomitant with the anticipated increase in the federal funds rate in June, the benchmark 10-year Treasury bill rate jumped over 75 basis points from the end of March (3.86%) to the end of June (4.62%). With the 10-year Treasury increasing significantly over the three-month period, interest rates for 30-year fixed mortgages experienced a similar trend increasing 85 basis points from the last week in March (5.40%) to the last week in June (6.25%)



In contrast to the relatively strong economic performance in the second quarter, the stock market experienced very modest increases. With uncertainty over the actions of the FOMC regarding interest rates, the Presidential election, and international events from the conflict in Iraq to oil prices, the stock market reflected those uncertainties. The NASDAQ experienced the largest gain at 2.7 percent, or an 11.2 percent annual rate (a.r.) during the second quarter, followed by the S&P 500 [ $\uparrow$  1.3%;  $\uparrow$  5.3%(a.r.)], the Dow Jones Industrial Average [ $\uparrow$  0.8%;  $\uparrow$  3.2%(a.r.)], and the Russell 2000 [ $\uparrow$  0.1%;  $\uparrow$  0.4%(a.r.)].



Similar to the national economy, which has achieved a sustainable growth rate of 4 percent, the region's economy also expanded during the year. Over the past year (May 2004 over May 2003), the Washington Coincident Index, which represents the current state of the Washington economy, increased 9.0 percent.



Consumer confidence picked up in April and May after lagging during the early part of the year and well above the level last year, and retail sales were up 9.0 percent for the year compared to 8.4 percent for the nation. While housing permits were down, housing prices continued to accelerate indicating a robust market.

Payroll employment has been the region's economic bright spot. For the past two months (April and May), the growth in payroll employment increased an average of almost 80,000 compared to the same period in 2003. Those increases were the highest among the 274 metropolitan regions in the country. The unemployment rate at 3.0 percent in May was the lowest among large metropolitan areas (population of 1 million or more).

In the near term, the region's economy is expected to outperform the nation's economy. According to the Center for Regional Analysis's Washington MSA Leading Index, the data suggest a strong second half of 2004 and with the recent performance in job growth, income derived from such growth will drive consumer spending.

## MONTGOMERY COUNTY ECONOMIC INDICATORS

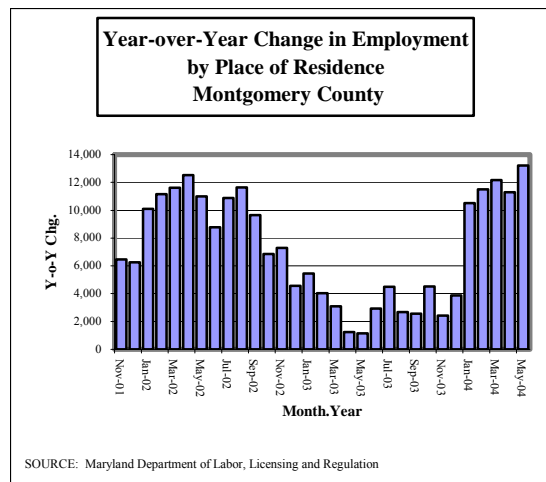
The County's economy during the first half of 2004 generally experienced significant improvement compared to the first six months of 2003. Employment among the County's residents grew significantly during the January-May period, non-residential construction rebounded during the first half of 2004 compared to the same period last year, retail sales improved over last year, and housing sales increased significantly during the first half of the year.

### *Employment Situation*

The employment situation in the County experienced two different patterns depending on the surveys conducted by the Maryland Department of Labor, Licensing and Regulation. Data based on the establishment survey show meager employment growth in 2003, the latest date

for which data are available. Total payroll employment grew 0.2 percent compared to 0.7 percent in 2001 and 0.9 percent in 2002. While total payroll employment experienced little growth, three sectors – financial activities, education and health services, and leisure and hospitality – added almost 3,700 jobs in 2003, which helped offset the loss of 3,000 jobs in the manufacturing, construction, and information technology sectors. The biggest disappointment in terms of job growth occurred in the professional and business services sector which added only 230 new positions in 2003. Because of the dramatic increase in federal procurement dollars into the County in federal fiscal year 2002, the expectations of such an increase would translate into a significant improvement in that sector as well as a turnaround in the information technology sector.

In comparison to the payroll data, resident employment provides a much different picture of the employment situation in the County. Since January, resident employment grew 12,000 on average per month compared for the first five months of 2003. While the data are based on a survey of households in the County rather than establishments, they provide a more current picture of the employment situation. While the resident employment data lack specificity on place of employment, recent data provided by the Montgomery County's Department of Park and Planning (MNCP&PC) suggest that nearly 60 percent of the County's residents also work in the County. That percentage is the highest among jurisdictions contiguous to the District of Columbia. Because of such a high percentage between working and living in the County, payroll employment in the County should experience a dramatic improvement in 2004 compared to 2003.

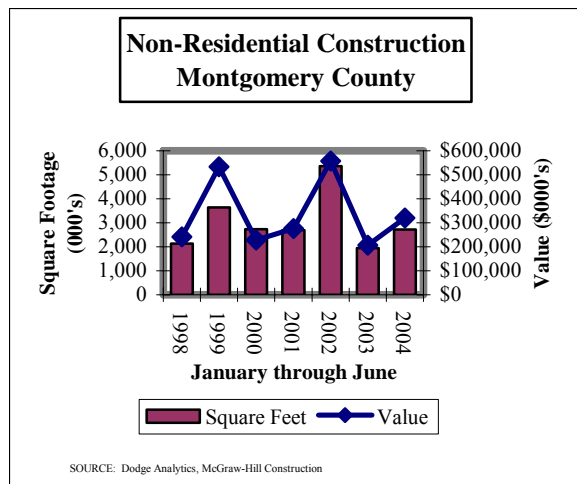


### **Construction Activity**

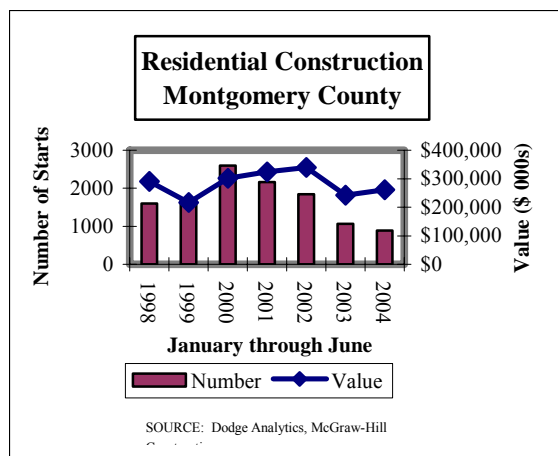
During the first half of 2004, construction activity in the County also experienced two entirely different trends. Construction of non-residential property grew both in terms of square footage and in added value compared to the first half of 2003. The amount of capacity added to the County's commercial real estate grew by almost 40 percent (2.7 million square feet) compared to 2003, and the value of construction grew an estimated 55 percent (\$320 million). A major contributor to the growth was the additional capacity of garage and service stations, which represented 37.5 percent of the additional non-residential construction space. Office and bank buildings represented an additional 22 percent of new construction. However, in terms of construction value, education and science laboratories contributed to nearly 30 percent of additional value and office and bank buildings 20 percent.

While non-residential construction improved in the County during the first half of 2004, the office vacancy rate on Class A property moderated. As of June 2004, the vacancy rate stood at 10.2 percent, down from the 10.9 percent in December.





The dramatic turnaround in non-residential construction was not matched by residential construction. In fact, through the first six months of 2004, the number of single-family homes built in the County declined 20.5 percent to slightly less than 830 units. However, that decline, which was the fourth consecutive decline since 2000, was not matched by a drop in construction value. In fact, the value of residential construction increased 8 percent during the first half of 2004 compared to the same period last year.

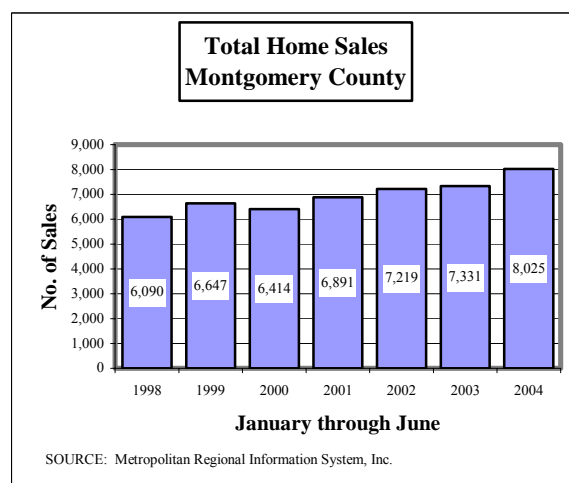


Essentially, while the construction of new units has steadily declined over the past four years, the average size of the new units has steadily increased from an average of

approximately 2,200 square feet in 2000 to approximately 3,200 square feet in 2004, an increase of 43.3 percent. Therefore, builders are constructing fewer but larger and more expensive single-family homes.

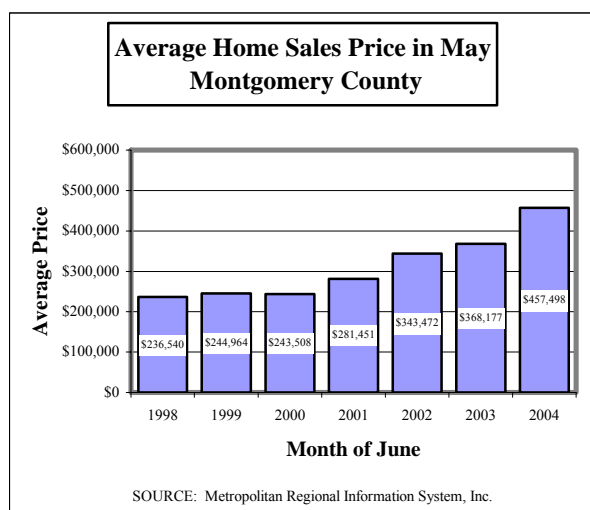
### *Residential Real Estate*

Homes sales in the County increased 9.8 percent during the first half of 2004 compared to the same period in 2003. Home sales of approximately 8,000 units to date have far exceeded sales during the previous six years. The dramatic rise in sales can be attributed to the expectation that mortgage rates will increase and that sales prices will continue to rise in the near term.



As stated previously, interest rates on 30-year fixed rate mortgages increased 85 basis points to 6.25 percent during the last week of June. The Mortgage Bankers Association (MBA) and the National Association of Home Builders (NAHB) expect mortgage rates to hold steady through the remainder of the year but increase during 2005 reaching 7.4 percent (MBA) or 7.5 percent (NAHB) by the fourth quarter of 2005. With the expectation that mortgage rates will increase in 2005 by 100 basis points, the significant growth in the sales of homes in the County may peak this year.

Along with the increase in sales, home prices in Montgomery County continued their historic rise. In June, the average selling price was almost \$460,000 compared to \$370,000 in June 2003 and \$245,000 in June 2000. The dramatic increase in home prices is attributed to two factors: demand is exceeding supply and builders are constructing larger and more expensive homes in part due to the limited land available for construction.

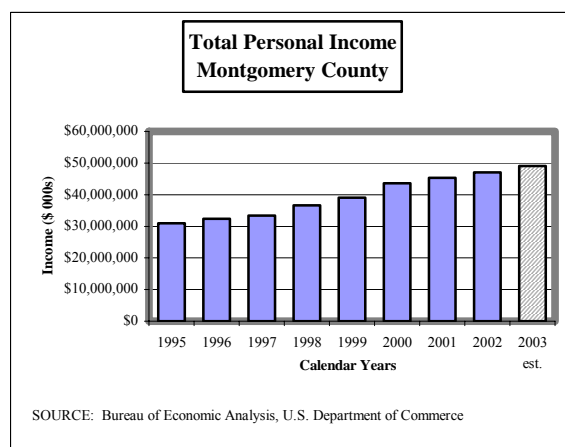


Data provided by MNCP&PC illustrate this recent trend. In 1990 the median price for a new single-family detached home was \$320,000 with a gross floor area (GFA) of 2,900, and the median prices of a new townhouse was \$160,000 with a GFA of 1,400. By 2004, it is expected that the median price for a new single-family detached home will increase to \$654,000 with a GFA of 3,600 and the median price for a new townhouse will reach \$440,000 with a GFA of 2,000. Essentially, the average price per gross floor area for a new single-family home increased from \$100 in 1990 to nearly \$185 in 2004. Over the same period, the average price per gross floor area

for a new townhouse increased from \$115 to \$220 – almost double within 14 years. If such trends continue in the near term, housing may become even less affordable in the County as increases in income will lag increases in home prices and interest rates.

### ***Personal Income***

The Bureau of Economic Analysis, U.S. Department of Commerce, recently revised annual personal income data for the County. As a result of that revision, total personal income was approximately \$47.1 billion in 2002, an increase of 3.8 percent over 2001, the latest date for which data are available. That annual increase was the smallest since 1997 when annual total personal income increased 3.1 percent.



However, based on the historic trend and recent performance in resident employment, total personal income may have reached \$47.0 billion by the end of this year. Although the expected increase in 2003 (↑ 4.3%) is slightly below the historical average of 5.8 percent between 1994 and 2002, it is greater than the increases in 2001 and 2002 (4.0% and 3.8%, respectively).



SELECTED ECONOMIC INDICATORS	Reporting Period	Current Period	Prior Year's Period	Year To-Date		
				2004	2003	2003
Leading Indicators						
National	May	0.5%		4.3%		3.0%
Washington MSA	May	-0.9%		3.0%		2.5%
Coincident Indicators						
National	May	0.3%		2.2%		1.1%
Washington MSA	May	1.9%		6.4%		1.9%
Consumer Confidence Index						
National	June	9.5%		24.2%		17.5%
South Atlantic Region	June	7.1%		25.3%		16.5%
Consumer Sentiment (University of Michigan)	June (p)	5.5%		13.0%		6.8%
Consumer Price Index						
All Items (nsa)						
National	June	3.3%		2.3%		2.3%
Washington - Baltimore CMSA	May	2.8%		2.3%		2.8%
Core CPI (nsa)						
National	June	1.9%		1.6%		1.5%
Washington - Baltimore CMSA	May	1.4%		1.4%		2.4%
Retail Trade						
National (sales - nsa)	June	7.6%		8.4%		5.6%
Washington MSA (sales - nsa)	May	6.3%		9.0%		6.5%
Maryland (sales tax)	May	11.6%		11.0%		3.5%
Montgomery County (sales tax)	May	7.8%		7.4%		4.0%
Employment						
National (household data - nsa)	June	139,861,000	138,468,000	138,192,000	137,097,000	137,736,000
- Percent Change		1.0%		0.8%		0.9%
Washington PMSA (household data - nsa)	May	2,814,036	2,730,102	2,798,574	2,717,060	2,763,091
- Percent Change		3.1%		3.0%		1.6%
Montgomery County (resident)	May	500,958	487,731	498,966	487,228	495,052
- Percent Change		2.7%		2.4%		1.1%
Montgomery County (payroll)*	Dec. '03	455,705	454,407	449,891	449,025	449,025
- Percent Change		0.3%		0.2%		0.7%
Unemployment						
National (nsa)	June	5.8%	6.5%	5.8%	6.2%	6.0%
Maryland (nsa)	June	4.2%	4.8%	4.1%	4.6%	4.3%
Washington PMSA	May	3.0%	3.5%	3.1%	3.6%	3.4%
Montgomery County	May	2.2%	2.6%	2.3%	2.7%	2.5%
Construction						
Construction Starts - Montgomery County						
Total (\$ thousand)	June	\$115,890	\$75,163	\$581,617	\$449,491	\$949,138
- Percent Change		54.2%		29.4%		-42.7%
Residential (\$ thousand)	June	\$88,423	\$50,095	\$261,602	\$242,717	\$567,664
- Percent Change		76.5%		7.8%		-29.3%
Non-Residential (\$ thousand)	June	\$27,467	\$25,068	\$320,015	\$206,774	\$381,474
- Percent Change		9.6%		54.8%		-55.5%
Building Permits (Residential)						
National	May (p)	182,900	167,081	810,619	718,138	1,862,365
- Percent Change		9.5%		12.9%		6.6%
Maryland	Apr	2,746	2,387	8,815	8,318	30,125
- Percent Change		15.0%		6.0%		2.8%
Montgomery County	Apr	565	327	1,473	1,848	4,590
- Percent Change		72.8%		-20.3%		-8.4%
Building Permits (Non-Residential)						
Montgomery County	June	186	151	959	811	1,798
- Percent Change		23.2%		18.2%		-3.2%
Real Estate						
National (saar)						
Sales	Apr	6,640,000	5,770,000	6,310,000	5,810,000	6,100,000
- Percent Change		15.1%		8.6%		9.6%
Median Price	Apr	\$176,000	\$164,100	\$172,075	\$161,300	\$170,000
- Percent Change		7.3%		6.7%		7.5%
Montgomery County						
Sales	June	2,073	1,783	8,025	7,331	16,534
- Percent Change		16.3%		9.5%		2.9%
Average Price	June	\$457,498	\$368,177	\$416,538	\$345,960	\$362,997
- Percent Change		24.3%		20.4%		13.2%
Median Price	June	\$377,900	\$305,000	\$337,703	\$277,667	\$295,500
- Percent Change		23.9%		21.6%		15.5%
Average Days on the Market	June	18	24	26	30	27

\* Year-to-Date data are for calendar years 2003 and 2002, respectively.

(p) = Preliminary

### METROPOLITAN AREA OFFICE MARKET

#### Office Vacancy Rate by Jurisdiction and Class, 06/04

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	15.25%	13.91%	4.60%	14.16%
Fairfax	13.47%	14.00%	5.29%	13.37%
Frederick	8.86%	1.09%	11.36%	2.11%
Alexandria/Arlington	9.62%	6.74%	6.36%	7.92%
<b>Montgomery</b>	<b>10.18%</b>	<b>9.13%</b>	<b>6.58%</b>	<b>9.36%</b>
District of Columbia	7.33%	6.28%	7.63%	6.97%
Prince George's	10.44%	10.44%	8.99%	10.21%
<i>Metropolitan Area</i>	10.45%	8.17%	7.07%	9.23%

#### Vacant Office Space Inventory by Jurisdiction and Class (sq.ft.)

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	867,625	492,572	25,609	1,385,806
Fairfax	8,634,791	4,325,532	174,142	13,134,465
Frederick	191,781	195,815	46,313	433,909
Alexandria/Arlington	2,348,226	1,750,536	452,542	4,551,304
<b>Montgomery</b>	<b>2,918,686</b>	<b>2,370,441</b>	<b>410,365</b>	<b>5,699,492</b>
District of Columbia	4,449,526	2,691,525	958,646	8,099,697
Prince George's	929,038	923,285	302,835	2,155,158
<i>Region</i>	20,339,673	12,749,706	2,370,452	35,459,831

#### Office Space Inventory by Jurisdiction and Class (sq.ft.)

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	5,691,006	3,541,680	556,426	9,789,112
Fairfax	64,084,312	30,886,041	3,292,233	98,262,586
Frederick	2,165,017	18,014,201	407,752	20,586,970
Alexandria/Arlington	24,399,935	25,974,455	7,115,617	57,490,007
<b>Montgomery</b>	<b>28,684,695</b>	<b>25,974,455</b>	<b>6,235,708</b>	<b>60,894,858</b>
District of Columbia	60,698,478	42,877,701	12,566,061	116,142,240
Prince George's	8,900,941	8,844,648	3,368,004	21,113,593
<i>Region</i>	194,624,384	156,113,181	33,541,801	384,279,366

#### Share of Office Space Inventory by Jurisdiction and Class

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	58.1%	36.2%	5.7%	100.0%
Fairfax	65.2%	31.4%	3.4%	100.0%
Frederick	10.5%	87.5%	2.0%	100.0%
Alexandria/Arlington	42.4%	45.2%	12.4%	100.0%
<b>Montgomery</b>	<b>47.1%</b>	<b>42.7%</b>	<b>10.2%</b>	<b>100.0%</b>
District of Columbia	52.3%	36.9%	10.8%	100.0%
Prince George's	42.2%	41.9%	16.0%	100.0%
<i>Metropolitan Area</i>	50.6%	40.6%	8.7%	100.0%

Note:

Office Space inventory includes leasable and owner-occupied space.  
 Totals exclude non-classified space.  
 Vacant means "direct vacant" and does not include sublease space.

Source:

Montgomery County Department of Planning, Research and Technology Center  
 Data compiled from Realty Information Group commercial space data file, 06/15/04

Updated June 16, 2004